



TaxNewsFlash Canada

Canada Moves Forward with Country-by-Country Reporting

August 8, 2016
No. 2016-39

Many Canadian companies of qualifying multinational corporate groups should prepare to meet new country-by-country reporting requirements now that Finance Canada has released draft legislation on these significant new rules. The rules, which are intended to enhance tax transparency and to provide adequate information to conduct transfer pricing risk assessments, were announced in the 2016 federal budget based on standards developed by the Organisation for Economic Co-operation and Development (OECD). This reporting will be required for taxation years beginning after 2015, with the first automatic exchanges of information between governments slated to begin by June 2018.

Although the 2016 federal budget provided some guidance on how Canada intends to implement these new requirements, the new draft legislation provides further clarification and details on important aspects of the new reporting regime. The draft legislation was released on July 29, 2016, and Finance Canada is accepting comments on its proposals until September 27, 2016.

Background

Country-by-country reporting of operational and financial information is part of transfer pricing reporting standards developed by the OECD to reduce base erosion and profit shifting (BEPS) by multinational enterprises.

The OECD released the final details for implementing a new country-by-country reporting plan in October 2015 under Action 13 of its BEPS project. This implementation package features model legislation and recommends a three-tiered approach that includes a country-by-country report (along with requirements for a master file and local files). This country-by-country report is intended to provide financial metrics for each

country in which the multinational enterprise operates, including revenue, income, taxes and indicators of economic activity.

Canada confirmed in its 2016 federal budget that it will implement country-by-country reporting and provided details on new requirements, including when Canadian parent entities of multinationals and Canadian resident entities need to report, the kinds of information expected to be in the country-by-country report, and the associated filing deadlines (see *TaxNewsFlash-Canada* 2016-17, "[Canada to Implement Country-by-Country Reporting in 2016](#)").

Who has to file?

The draft legislation confirms the 2016 federal budget's announcement that Canadian-resident ultimate parent entities of multinationals with consolidated revenues of €750 million or more during the preceding fiscal year will be required to file a country-by-country report with the CRA. However, Finance Canada has now provided definitions and further clarity on which entities must file a report.

The legislation, which is in proposed section 233.8 of the *Income Tax Act*, defines a multinational enterprise group as two or more business entities that are required to prepare consolidated financial statements for financial reporting purposes under applicable accounting principles (or would be required to do so if equity interest of any of the business entities were traded on a public securities exchange) where the business entities operate in more than one jurisdiction.

A Canadian-resident "constituent entity" of a multinational enterprise group must also file the report in certain circumstances. A constituent entity is a business entity within a multinational enterprise group that is included in the group's consolidated financial statements for financial reporting purposes (or would be required to be included if equity interests in any of the group's business entities' were traded on a public securities exchange). It also includes any business entity that is excluded from the group's consolidated financial statements solely for size or materiality reasons.

Specifically, a Canadian-resident constituent entity must file this report in Canada where:

- The ultimate parent entity is not obligated to file a country-by-country report in its jurisdiction of tax residence
- The ultimate parent entity's jurisdiction of tax residence does not have an agreement for the automatic exchange of country-by-country reports with Canada as of the required filing date (a "qualifying competent authority agreement"); or
- Finance Canada has notified the constituent entity of a systemic failure, which can arise if there has been a suspension of automatic exchange for a qualifying competent

authority agreement with the jurisdiction of the ultimate parent entity or the jurisdiction of the ultimate parent entity has persistently failed to automatically provide country-by-country reports in its possession to Canada).

Where there is more than one constituent entity of a multinational enterprise group in Canada to which the filing requirements noted in the above paragraph apply, the draft legislation allows one of those constituent entities to be designated to file on behalf of all such constituent entities in the multinational enterprise group. This designation must be made on or before the report's filing date.

Notwithstanding the above, a Canadian-resident constituent entity will not be required to file a country-by-country report if a surrogate parent entity files the country-by-country report for the multinational enterprise group on behalf of the ultimate parent entity. For this exception to apply, the surrogate parent entity:

- Must have country-by-country report filing requirements in its jurisdiction of tax residence
- Must have a qualifying competent authority agreement in effect to which Canada is a party in its jurisdiction of tax residence
- Must be in a jurisdiction of tax residence that is not in a position of systemic failure; and
- Must have notified its jurisdiction of tax residence that it will be filing a country-by-country report in place of the ultimate parent entity.

Where an ultimate parent entity is a partnership, the proposed legislation specifies that, for country-by-country reporting purposes, it is deemed to be resident in another jurisdiction if it is resident there for tax purposes under that jurisdiction's laws. In any other case, an ultimate parent entity that is a partnership will be resident in the jurisdiction under the laws of which it was organized.

KPMG observations

It does not appear that Finance Canada incorporated more specific comments and submissions that they received from certain taxpayers prior to the release of these draft proposals. This is not surprising given the fact that Finance Canada had previously indicated that they wanted Canada's legislation to follow the OECD guidelines as much as possible, leaving little room for country-specific amendments.

Consistent with the OECD's recommendations outlined in Action 13, the draft legislative proposals specify that multinational enterprise groups with consolidated group revenue of less than €750 million during the immediately preceding fiscal year are considered excluded multinational enterprise groups for the application of the proposed Section 233.8 of the Act. However, no Canadian dollar equivalent of this revenue threshold has been proposed by Finance Canada and it remains to be seen how companies that are

within reach of the €750 million threshold will respond to the country-by-country reporting requirements in Canada.

The intention of the proposed section 233.8 of the Act appears to be to subject any Canadian constituent entities that are part of a multinational enterprise group that is at or above the €750 million threshold to country-by-country filing requirement in some capacity. This is also applicable to Canadian constituent entities whose ultimate parent entity or surrogate parent is in a country that is implementing country-by-country reporting at a later date, such as the U.S. that requires country-by-country reports to be filed for taxation years beginning on or after June 30, 2016.

The IRS and the U.S. Treasury have announced that they intend to allow ultimate parent entities of U.S. multinational enterprise groups to file, on a voluntary basis, country-by-country reports for reporting periods that begin on or after January 1, 2016 to align with the first reporting period recommended by the OECD and implemented by most countries adopting country-by-country reporting requirements, including Canada. In a release dated June 29, 2016 and titled *Guidance on the implementation of country-by-country reporting*, the OECD has recommended that these voluntary parent surrogate filings be respected, under a number of conditions, so as to prevent local filings in many jurisdictions (like Canada) implementing country-by-country reporting requirements for reporting periods starting on or after January 1, 2016.

The draft legislative proposal is silent on the OECD-recommended mechanism to be followed to notify tax authorities about the entity within a multinational enterprise group, whether the ultimate parent entity or the surrogate parent, that is responsible for filing the country-by-country report.

What has to be filed and how?

The draft legislation does not provide details on the contents of the country-by-country report. The draft legislative proposals only state that the report must be in the prescribed form and filed in the prescribed manner.

KPMG observations

Based on Finance Canada's recent release and on the 2016 federal budget, there is no reason to believe that the Canadian country-by-country report will deviate from the OECD's recommendations. Given the limited guidance in the draft legislative proposals regarding data sources and requirements, Canadian taxpayers should look to the OECD's guidance to determine how to report information. The OECD suggests that the country-by-country report should include the global allocation of the following information on a country-by-country basis:

- Related and unrelated party revenues
- Profit before tax
- Income taxes paid and accrued
- Stated capital
- Accumulated earnings
- Number of employees
- Tangible assets
- The main activities of each of the multinational enterprise group's entities.

In addition, the mechanism for filing the country-by-country report is unclear in the draft legislation. We expect that the CRA will release a prescribed country-by-country form that should provide further clarification on the required information.

Compliance with the draft legislative proposals will require that country-by-country reports filed by multinational enterprise groups be aligned with the prescribed Canadian country-by-country report or with substantially similar reports to the Canadian country-by-country report that are required to be filed in other jurisdictions. Considering that certain other jurisdictions may adopt domestic country-by-country reporting requirements that may slightly vary from the OECD guidance, it remains to be seen whether such differences could fall short of the Canadian reporting requirements.

From a broader transfer pricing transparency perspective, Finance Canada has not released draft legislation for the master file and local file documentation requirements that the OECD recommended along with the country-by-country reporting requirement as part of Action 13. Since many impacted Canadian based multinational enterprises will have subsidiaries in jurisdictions that may have master file/local file requirements, these requirements need to be monitored and it would be prudent to prepare a master file at the Canadian parent level to ensure consistency and accuracy across the group.

What is the filing deadline?

The draft legislation confirms details announced in the budget concerning the filing deadline. Under the new regime, country-by-country reports must be filed within 12 months after the last day of the multinational enterprise group's reporting fiscal year that begin on or after January 1, 2016.

However, if Finance Canada notifies a constituent entity of a systemic failure, the filing deadline is on or before the later of 30 days after receipt of such notification, or 12 months

after the last day of the group's reporting fiscal year. This provision is intended to address situations where a constituent entity may be informed of systemic failure beyond the period within which it could meet the 12-month deadline.

The draft legislative proposals also provide for a penalty for failure to file the country-by-country report by proposing changes to current paragraph 162(10)(a) of the Act dealing with penalties for failure to file certain information returns including forms T106.

KPMG observations

Since the filing deadlines are relative to the multinational enterprise group's fiscal year-end, Canadian taxpayer's country-by-country report filing deadline may not align with their fiscal year-end.

Given the potential obstacles in gathering the required data and the need to ensure consistency of information used for transfer pricing purposes, Canadian taxpayers may want to complete the country-by-country report before their contemporaneous transfer pricing documentation and tax return filing deadlines, particularly in the first year.

We can help

KPMG can assist you at every phase of your country-by-country reporting strategy. Whether you are looking at performing a preliminary readiness assessment, a blueprinting exercise to assist in defining the scope and country-by-country factors, a strategic risk assessment relying on analytics, or an end-to-end country-by-country reporting project, we can bring experience and leading practices from our national and global network. We can also assist clients on projects through the use of our proprietary technology tool KPMG LINK Country-by-Country Reporting, a web-based application to capture, analyze and report data.

For more details on these developments and their potential impact, contact your KPMG adviser or one of the following members of our transfer pricing team:

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